Report on Commissioner of Revenue's Use of Additional Reporting Requirements

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Introduction

In 2017, the Massachusetts Legislature amended M.G.L. c. 62C, § 8 to allow the Commissioner of Revenue (Commissioner) to impose reporting requirements that differ from those required by the Internal Revenue Code (IRC). *See* St. 2017, c. 47, § 34. Pursuant to St. 2017, c. 47, § 125, the Commissioner is issuing this report on the use of that authority. The report provides an explanation for the change made and the financial impact of an additional reporting requirement.

Explanation of Change

Following the amendment of M.G.L. c. 62C, § 8, the Commissioner issued TIR 17-11 announcing an additional reporting requirement for third party settlement organizations (TPSOs). TPSOs are generally online payment intermediaries, such as PayPal, that transmit payments between buyers and sellers of goods and services. Current federal law requires a TPSO to report the gross amount it pays in settlement to a payee only when such payments exceed $20,000 in over 200 transactions during a calendar year.[1] *See* IRC § 6050W(e). A TPSO is required to report these amounts using Form 1099-K.

In TIR 17-11, the Commissioner announced that TPSOs must report the gross amount paid in settlement to a payee when such amount is $600 or greater and is subject to taxation under M.G.L. c. 62, regardless of the number of transactions between the TPSO and the payee. In 2020, the Commissioner promulgated 830 CMR 62C.8.1, "Massachusetts Reporting Requirements for Third Party Settlement Organizations," which codified this requirement and provided compliance rules specific to payees.

The Commissioner lowered the reporting threshold for gross payments in settlement made by TPSOs to increase transparency and tax compliance principally among individuals selling goods and services who receive such payments from TPSOs. Taxpayer compliance in reporting taxable income is significantly higher when such income is subject to an information reporting requirement.[2] In recent years, "gig economy" platforms, where a TPSO generally serves as a payment intermediary connecting buyers and sellers of services and goods, have grown substantially. The use of TPSOs to transmit payments more generally has also increased. Under the federal TPSO reporting threshold, gross payments in settlement by a TPSO to an individual selling goods or services would not be subject to an information reporting requirement unless such payments exceeded $20,000 effectuated through at least 200 transactions. This threshold resulted in a reporting gap whereby much of the income earned by these individuals would not be subject to an information reporting requirement.

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[1] The American Rescue Plan Act, P.L. 117-2, lowers the federal TPSO reporting threshold to gross payments in settlement to a payee exceeding $600 in a calendar year, regardless of the number of transactions, starting with payments in settlement made during the 2022 calendar year.

[2] See Treasury Inspector General for Tax Administration's "Expansion of the Gig Economy Warrants Focus on Improving Self-Employment Tax Compliance" report at https://www.treasury.gov/tigta/auditreports/2019reports/201930016fr.pdf, which explains that taxpayer compliance is at 93% when amounts are subject to information reporting. In contrast, taxpayer compliance is at 37% when amounts are not subject to an information reporting requirement.

In evaluating where to set the TPSO reporting threshold, the Department of Revenue (DOR) looked to the rules for reporting payments to independent contractors on Form 1099-MISC. Payments to independent contractors are required to be reported on Form 1099-MISC when such payments equal or exceed $600 in a calendar year. DOR ultimately concluded that gig economy workers and other independent contractors should be subject to the same reporting threshold. This modification is the only additional reporting requirement the Commissioner has imposed to date under M.G.L. c. 62C, § 8.

Financial Impact to the Commonwealth of the Changes

DOR conservatively estimates that the change to the TPSO reporting requirement has increased reported net income by a total of roughly $137M for 2017, the first year to which the TPSO threshold changes applied, and 2018. This estimate is based on the lower of taxpayers' gross receipts reported on Form 1099-K and the sum of their net profits reported on schedules C, E, and X and allowed for deductions. Applying the Part B personal income tax rate in effect for each year to the reported $137M in additional net income, DOR estimates a revenue increase of approximately $7M for each of the 2017 and 2018 tax years.

This estimate is based on income reported that DOR was able to match with a Form 1099-K. Because of the large amount of 1099-K data that is either missing or deficient, the actual financial impact of the lower reporting threshold could be significantly higher.